VZCZCXRO1897
OO RUEHLMC
DE RUEHTG #0903/01 2522122
ZNR UUUUU ZZH
O 092122Z SEP 09
FM AMEMBASSY TEGUCIGALPA
TO RUEHC/SECSTATE WASHDC IMMEDIATE 0631
INFO RUEHZA/WHA CENTRAL AMERICAN COLLECTIVE IMMEDIATE
RUEAIIA/CIA WASHDC IMMEDIATE
RUCPDOC/DEPT OF COMMERCE WASHDC IMMEDIATE
RUEATRS/DEPT OF TREASURY WASHDC IMMEDIATE
RHEFDIA/DIA WASHINGTON DC IMMEDIATE
RUEIDN/DNI WASHINGTON DC IMMEDIATE
RUEHLMC/MILLENNIUM CHALLENGE CORP WASHINGTON DC IMMEDIATE 1197
RHEHAAA/NATIONAL SECURITY COUNCIL WASHINGTON DC IMMEDIATE
RUMIAAA/USSOUTHCOM MIAMI FL IMMEDIATE

UNCLAS SECTION 01 OF 03 TEGUCIGALPA 000903

SENSITIVE
SIPDIS

STATE FOR EXIM/MICHELE WILKINS

E.O. 12958: N/A
TAGS: BBSR ECON EFIN HO KDEM PGOV
SUBJECT: TFHO1: DE FACTO REGIME'S POSITION ON PUBLIC
FINANCES

REF: A. TEGUCIGALPA 808
¶B. TEGUCIGALPA 771
¶C. TEGUCIGALPA 697

¶1. (U) Summary: On August 28, the Ministry of Finance of the de facto regime published an advertisement in the major dailies describing the current conditions of public finances in the country and actions the de facto regime is taking to manage public finance during the rest of the year. The announcement details the impact of the financial crisis and criticizes the Zelaya administration for mismanagement. It describes actions taken by the de facto regime to restructure government finances and measures to control future disbursements. The announcement closes with the statement that the 2010 budget will be delivered no later than September 15th (a dig at the Zelaya administration, which failed to deliver a 2009 budget). End Summary.

Impact of the International Financial Crisis

¶2. (U) On August 28, the Ministry of Finance of the de facto regime published a two-page advertisement in major dailies under the title, "What did we receive (i.e. inherit)? Where are we? Where are we going?" The announcement describes the impact of the crisis on Honduras's already weak economy, noting that the regime inherited an economy that was suffering from reduced remittance flows, lower exports and falling investment. This had obligated the Central Bank of Honduras (BCH) to lower its growth estimate for 2009 to only 2 percent. (Note: The de facto regime later revised the GDP estimate downward to a loss of 1 to 2 percent. End note.) The announcement asserts that although the Zelaya administration prepared a plan to address the financial crisis, this plan was never implemented. It states that although the de facto regime has prepared a 2009 budget that addresses the major challenges facing the economy, the future remains uncertain and Honduras remains at risk in the face of the financial crisis.

¶3. (U) The announcement asserts that policies of the Zelaya administration made matters worse, increasing unemployment and reducing investment. This lower level of economic activity has translated into less income for families and businesses, affecting the government's tax collections. The one bright spot was inflation of only 4 percent, which is attributed to the private sector's decision not to raise prices of the basic food basket. (Comment: Lower inflation was more likely caused by lower prices for key imported

commodities such as energy. End comment.)

What They Received

¶4. (U) The announcement states that public finances began to weaken in 2006 (at the start of the Zelaya administration) due to deterioration of the finances of state-owned businesses as a result of the increase in the number of employees combined with high energy and fuel subsidies. As a result of these practices, public savings were diminished, which greatly impacted public investment and poverty reduction programs. Salaries and wages in the first half of 2009 increased 19 percent compared to the first half of 2008, while several institutions, such as the National Institute of Statistics and Presidential Palace (both highly involved in President Zelaya's effort to conduct a constitutional survey), spent their entire 2009 budget in the first six months of the year.

¶5. (U) The announcement cites a tremendous increase in domestic public debt from approximately USD 317 million as of December 2007 to USD 847 million on April 2009. Due to Zelaya administration strategies, almost USD 400 million of debt was coming due in the second half of 2009 while the National Treasury had unpaid bills of USD 185 million. The announcement further states that the Zelaya administration withdrew almost USD 300 million from the National Treasury without any budget allocation to control the use or destination of the funds. This amount, the announcement states, does not include salaries with no budget allocation

that would increase the amount to almost USD 800 million, nor does it include large withdrawals of cash from BCH by employees of the Office of the Presidency.

Where They Are

¶6. (U) After congratulating itself on passing the 2009 budget and providing greater transparency to the Honduran people, the de facto regime notes that it expects the consolidated fiscal deficit to reach 2.4 percent of GDP. The announcement highlights new controls the regime has placed on the use of public funds, including requiring two signatures for each withdrawal, no transfers between public sector institutions and limiting cash withdrawals to about USD 10,000. Further, the regime plans to retain an audit firm with an international reputation to perform a forensic audit of 2008 and first half 2009 results. Expenses for the central government will be cut 10 percent for the remainder of the year, while the decentralized institutions will be cut 20 percent.

¶7. (SBU) The new budget contemplates the issuance of USD 340 million in government bonds, of which USD 140 million was placed in the first quarter of the year. (Comment: Sources note that an additional USD 143 million was placed privately to banks in August after the Central Bank increased obligatory investments. End comment.) In addition, about USD 200 million of short term debt held by the central bank was converted to a 10-year loan, while over USD 180 million of maturing debt will be rolled over, saving a cash outflow of USD 380 million. (Note: Most of this debt is held by government pension funds. End Note.)

¶8. (U) The announcement states that revenues for the central government are expected to decline 7.0 percent, equivalent to 1.7 percent of GDP, while the sharp use of the budget axe will keep expenses flat, resulting in a fiscal deficit of 4.2 percent of GDP compared to the original projection of 2.5 percent.

Where They Are Going

¶9. (U) The announcement closes by stating that the new 2010 budget will be presented no later than September 15, as required by law. The regime asserts that this new budget will be highly compromised by the expansionist decisions taken by the Zelaya administration, but pledges to be honest with the public about the state of public finances. The National Congress and the people, the regime asserts, will recognize that it is telling the truth.

Comment

¶10. (SBU) Although this is a self-serving document, most of the factual assertions appear to be correct (to the extent they can be verified). In strictly technical terms, the de facto regime has put together a strong economic team to address the crisis, including Gabriela Nunez as Minister of Finance (former Minister of Finance in the Flores administration, former president of the central bank in the Zelaya administration and presidential candidate in the 2005 primaries) and Sandra Midence as president of the central bank (vice minister of finance in the Flores administration and vice president of the central bank in the Zelaya administration), plus Hugo Castillo, who has stayed on as vice minister of finance, and Angel Arita, a senior central bank official who was promoted to vice president of the central bank. They appear to have successfully addressed the looming liquidity crisis created by short-term overhang of maturing debt in excess of USD 500 million, but USD 158 million maturing in February 2010 still remains a potential concern. Additional financing may be required to close the budget gap due to the lack of budget support from the international community, although the amount is not large (under USD 100 million). The announcement is obviously an attempt to build credibility with the domestic audience, but with an eye to the broader international audience as well.

¶11. (U) An informal English translation of the original document, which includes graphs and tables, can be obtained from Embassy Tegucigalpa Treasury Officer Victor Bolles at bollesvc@state.gov.
LLORENS